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Servicer Evaluation: Berkadia Commercial Mortgage LLC

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Servicer Evaluation: Berkadia Commercial Mortgage LLC

Ranking Overview

Commercial primary	
Overall ranking	STRONG
Subranking	
Management and organization	STRONG
Loan administration	STRONG
Outlook	Stable
Commercial master	
Overall ranking	STRONG
Subranking	
Management and organization	STRONG
Loan administration	STRONG
Outlook	Stable
Commercial special	
Overall ranking	ABOVE AVERAGE
Subranking	
Management and organization	ABOVE AVERAGE
Loan administration	ABOVE AVERAGE
Outlook	Negative
Financial position	SUFFICIENT

Key Ranking Factors

- Experienced and tenured senior management team;
- Strong audit and quality control (QC) environment;
- Proactive, well-documented compliance/governance and internal controls;
- Demonstrated track record with a diverse constituency of investor and property types and a strong commitment to primary servicing;
- Efficient use of technology systems and offshoring operations; and
- Continued low levels of special servicing, declining master servicing volumes, and the company's uncertain growth strategy for both lines of business.

Opinion

Standard & Poor's Ratings Services' rankings on Berkadia Commercial Mortgage LLC (Berkadia) are STRONG as a commercial mortgage primary servicer and master servicer and ABOVE AVERAGE as a commercial special servicer. On Oct. 30, 2015, we affirmed these rankings (please see "Berkadia Commercial Mortgage LLC Commercial Rankings

Affirmed; Special Servicer Ranking Outlook Revised To Negative"). The ranking outlook for special servicing is negative, while the ranking outlooks for primary and master servicing are stable.

Our overall rankings on Berkadia's primary and master servicing capabilities reflect our view of its well-controlled, efficient operations that cover domestic offices, and a fully owned operation in Hyderabad, India, to achieve strong operating results. Berkadia's special servicing ranking reflects its commitment to maintaining the appropriate staffing for its current portfolio, policies and procedures, and compliance efforts despite the continued low level of special servicing volume and staffing after contributing its legacy commercial mortgage-backed securities (CMBS) special servicing portfolio to KeyBank Real Estate Capital (KeyBank) in 2013 as part of a larger transaction.

Berkadia is the third-largest U.S. commercial servicer based on unpaid principal balance (UPB) and, as is the case for many of the large servicers, has used offshore resources to manage costs. The primary servicing portfolio is diverse by property and investor type, including CMBS, government-sponsored entities (GSEs), life insurance company mortgages, fee-for-service, warehouse, U.S. Department of Housing and Urban Development, Ginnie Mae, and private-label servicing. While the primary servicing portfolio shrank a few years back from run-off, volume began increasing in 2012, and the UPB has remained relatively steady since, approximating \$225 billion as of June 30, 2015.

We believe Berkadia is an effective master servicer, despite its continued declining volume. As of June 30, 2015, Berkadia monitored 20 subservicers, who serviced 479 loans containing \$5.3 billion in UPB. However, the subservicer portfolio has continued to decline in recent years as loan run-off has greatly exceeded new loan activity. We view the lack of growth as a longer-term concern for the master servicing ranking, especially if the larger industry competitors continue to dominate the market. Nonetheless, we expect Berkadia to continue to demonstrate its ability to selectively and effectively acquire master servicing rights when strategically important or when borrower relationships come into play.

Overall, staffing levels have been well managed, in our opinion, and Berkadia continues to focus on cost-to-service, process improvements, and technology advancements as it broadens its fee-for-service initiatives. High levels of experience and tenure are also evident among its various servicing platforms, as is well-integrated technology. Finally, Berkadia makes efficient use of its offshore Hyderabad office to handle a high volume of back-office tasks at lower costs than its U.S. operations, allowing U.S. servicing personnel to focus on asset and portfolio management, client services, and compliance.

While special servicing experience and tenure have remained consistent since the KeyBank transaction, the uncertain future of the business and limited staffing depth no longer support a STRONG management and organization subranking for special servicing. Consequently, on Oct. 30, 2015, we lowered the subranking to ABOVE AVERAGE.

Outlook

Our outlook for the primary servicing ranking is stable. Berkadia has a long and successful track record servicing commercial and multifamily mortgage loans. We believe the company has a highly diverse portfolio in terms of investor type and asset mix, both geographically and by property type. Furthermore, Berkadia has demonstrated its ability to meet multiple reporting requirements for CMBS, GSEs, life companies, and other third parties for many years.

Berkadia's primary servicing growth plans and strategic objectives are reasonable, and it has consistently demonstrated a commitment to investing in technology resources and continuous process improvement.

The outlook for the master servicing ranking is stable. While the primary servicing infrastructure is suitable to handle the master servicing functions and the increased fee-for-service loan volume has resulted in stable primary servicing portfolio levels, the lack of loan growth in the master servicing portfolio is a longer-term ranking concern, particularly as the CMBS markets have been active and growing. Management has indicated that it continues to solicit primary and master servicing assignments as opportunities meet their disciplined investment criteria, but so far these assignments haven't completely mitigated portfolio run-off. We will continue to monitor the status of its master servicing portfolio as significant future volume decreases could result in an outlook or ranking revision.

The outlook for the special servicing ranking is negative. We believe Berkadia has maintained adequate staffing for its current portfolio, special servicing systems, and procedures since the aforementioned KeyBank transaction, supporting the current overall ranking level at this time. However, if Berkadia doesn't obtain meaningful new special servicing assignments during the intermediate term, there is the potential that we will lower our ranking.

Key Changes

- Named a new chief executive officer;
- Promoted a veteran servicing executive of the company to president of Berkadia Commercial Real Estate Services;
- Acquired Keystone Commercial Capital, a commercial mortgage banking company, with a \$2 billion servicing portfolio;
- Continued to invest in servicing technology, upgrading its servicing system to Strategy 17.3 in late 2014 and migrated to 17.6 in the third quarter of 2015 alongside other enhancements to its insurance monitoring;
- Opened a disaster recovery business continuity site in Pune, India in April 2014;
- Relocated its domestic disaster recovery and business continuity center to TierPoint in Norristown, Pa. in December 2014; and
- Experienced further run-off in both its master and special servicing portfolios.

Profile

Servicer Profile	
Servicer name	Berkadia Commercial Mortgage LLC
Primary servicing location	Ambler, Pa.
Parent holding company	Berkadia Proprietary Holding LLC
Servicer affiliates	Berkadia Services India Private Ltd., Berkadia Commercial Mortgage Inc., Berkadia Capital Markets LLC, and Hendricks-Berkadia LLC
Loan servicing system	Strategy v 17.6

Berkadia is a commercial real estate company with integrated lines of business, including commercial loan servicing, loan origination, and investment sales. In 2014, the company originated more than \$13.1 billion in GSE, institutional, CMBS, and proprietary mortgage lending, and management expects 2015 origination volumes to exceed 2014 levels. In addition, during 2014, the investment sales division completed 428 transactions that exceeded \$4 billion in volume.

Management expects 2015 investment sales volume will exceed \$5 billion.

Table 1

Portfolio Overview										
	June 30, 2015		Dec. 31, 2014		Dec. 31, 2013		Dec. 31, 2012		Dec. 31, 2011	
	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.
Primary loans	224,523	21,080	229,325	22,204	227,479	24,004	182,481	23,284	163,796	21,902
Master (SBO) loans	5,258	479	6,017	625	7,235	1,016	9,585	1,422	12,062	1,828
Total servicing	229,781	21,559	235,342	22,829	234,713	25,020	192,066	24,706	175,858	23,730
Average loan size	10.7	--	10.3	--	9.4	--	7.8	--	7.4	--
Special servicing										
Loans	8	22	3	17	20	21	867	85	1,469	189
REO properties	1	3	0	--	0	--	716	30	1,213	116
Total special servicing	9	25	3	17	20	21	1,583	115	2,682	305

SBO--Serviced by others. REO--Real estate owned.

Berkadia's commercial servicing division was formed in September 2009 as a joint venture between Berkshire Hathaway Inc. (BRK) and Leucadia National Corp. (LUK). Berkadia acquired the U.S. servicing and mortgage banking operations of its predecessor Capmark Financial Group Inc. (Capmark) as part of Capmark's bankruptcy reorganization in December 2009. In the U.S., primary and master servicing operations are mainly conducted in Ambler, Pa., with additional offices in Tempe, Ariz.; Salt Lake City; St Louis; and New York. However, the bulk of the firm's servicing employees are based in Hyderabad, India, where many back-office operations are performed. The special servicing staff is modest and operates out of Irvine, Calif. and Ambler, Pa.

Table 2

	Unpaid principal balance (mil. \$)	Loans (no.)	Unpaid principal balance (%)	Loans (%)
CMBS/CDO/ABS	59,839	6,351	26.0	29.5
Other third-party investors	130,033	10,283	56.6	47.7
Commercial bank/savings Institutions	1,245	94	0.5	0.4
Fannie Mae/Freddie Mac	20,717	1,763	9.0	8.2
FHA/Ginnie Mae	8,419	1,626	3.7	7.5
Life insurance companies	8,852	1,373	3.9	6.4
Loans held in warehouse	-	-	0.0	0.0
Own or parent's balance sheet	677	69	0.3	0.3
Total	229,781	21,559	100.0	100.0

Table 2

Berkadia Commercial Mortgage LLC--Total Portfolio By Investor Type(i) (cont.)

(i)As of June 30, 2015. CMBS--Commercial mortgage-backed securities. CDO--Collateralized debt obligation. ABS--Asset-backed securities. FHA--Federal Housing Administration.

Berkadia has been a market leader in leveraging its technology infrastructure and cost advantages of its offshore operations to become the "servicer's servicer," particularly in providing servicers with "non-client facing" outsourcing support to allow clients to focus on their core competencies. Its fee-for-service loan portfolio includes both CMBS (\$73 billion UPB at March 31, 2015) and non-CMBS loans (\$61 billion UPB at March 31, 2015).

Management And Organization

Our subrankings on Berkadia's management and organization are **STRONG** for primary and master servicing. We based the subrankings on our view of the company's long, successful track record servicing multifamily/commercial real estate loans, its experienced management team, good leverage of technology, and sound audit and control environment.

Our subranking on Berkadia's management and organization for special servicing is **ABOVE AVERAGE**. We based the subranking on our view of the servicer's good leverage of technology, adequate control environment, and strong training program. The modest staffing and uncertain future growth plans of the special servicing platform is the key distinguishing factor that limits the special servicing management and organization subranking relative to primary and master servicing.

Staff depth and organizational effectiveness

Berkadia continues to maintain a focus on growth in its primary servicing portfolio, while its master and special servicing units have continued to shrink. Of the more than 748 total employees that make up the primary and master servicing operations, approximately 520 are based in India. The special servicing team has seven employees, who are based in Irvine, Calif. and Ambler, Pa.

For primary and master servicing, we believe Berkadia has a highly experienced management team with good depth and tenure along with a well-trained staff (see table 3). The company continues to leverage its Hyderabad office for cost-benefit and operational efficiencies of selected high volume servicing tasks. The Ambler office oversees and monitors the performance of the Hyderabad office.

The organizational structure is such that primary and master servicing employees have parallel reporting to functional managers in the U.S. and India, aligning the goals and interests of the Hyderabad staff with their Ambler counterparts. The overall primary and master servicing employee turnover rate in 2014 was 24%, up from 18% in 2013. The primary servicing turnover rate for staff declined through the first half of 2015, totaling 10%. Special servicing experienced no turnover of its small staff during the six months ending June 30, 2015.

While the primary servicing turnover rates are higher than most servicers in the U.S., they are lower than India standards and indicate an effective employee retention program, in our view. By management's measurement, Berkadia achieved a controllable turnover level (employee departures for anything other than family reasons or

returning to school) of 12.3% during 2014, which is slightly above its goal of below 12.0%.

Table 3

Industry Experience/Company Tenure(i)								
	Senior managers		Middle managers		Asset managers		Staff	
	Industry experience	Company tenure	Industry experience	Company tenure	Industry experience	Company tenure	Industry experience	Company tenure
Primary	24	14	19	12	--	--	6	5
Master	24	14	19	12	--	--	6	5
Special	27	18	27	12	26	17	24	16

(i)As of June 30, 2015.

Berkadia established Berkadia Services India (BSI) 12 years ago and gradually has migrated specific loan servicing processes to the Hyderabad office, including:

- Loan boarding;
- Document imaging and workflow;
- Tax, insurance, and escrow administration;
- Reserve administration;
- Payoff statements;
- Bank account reconciliations;
- Investor reporting;
- Surveillance and watchlist reporting; and
- Financial statement and rent roll analysis.

We believe Berkadia has continued to develop its Hyderabad office by continuing essential training programs, installing QC measures, and methodically shifting servicing tasks.

The servicing group includes both primary/master servicing and special servicing. For primary/master servicing, the client services group handles new loan boarding, shared services, selected data management activities, special requests, and client relations. The agency and life company groups oversee their respective investor portfolios; the banking group handles payment processing, cash management, bank account reconciliations, investor accounting, and investor reporting. The servicing operations group handles financial statement analytics, reserves, escrow administration, collateral activities, surveillance, and special servicing. Responsibilities for each task are distributed between domestic and offshore staff and are specific to each function.

Berkadia has sufficient resources for its workload as measured by its loans-to-employee (LPE) ratio for its primary/master servicing unit (see table 4). The LPE ratio is driven primarily by the high staffing level in Hyderabad, which is beneficially offset by a much lower overseas operating cost. As a result, we believe the June 30, 2015, LPE ratio of 29, which has declined in recent years as loan complexity has increased, indicates that Berkadia has adequate capacity for additional portfolio growth.

Table 4**Berkadia Commercial Mortgage LLC--Primary/Master Servicing Employee Ratio**

	Loans per employee
June 30, 2015	29
Dec. 31, 2014	31
Dec. 31, 2013	37
Dec. 31, 2012	40
Dec. 31, 2011	40
Dec. 31, 2010	43

Training

Berkadia maintains a strong commitment to training and professional development, and it has a well-defined training program. Features of Berkadia's training program include the following:

- During 2014, the company hired a corporate trainer, who partners with the respective departmental business leads to assess yearly training needs.
- A performance, development, and planning program (PDP) is administered by the human resources department, facilitating the relationship between career development, achievements, and compensation.
- The Berkadia University website, which provides employees access to over 4,000 training topics, supports employees' learning and development requirements. Training covers system and subject-matter specific training, CampusMBA, mortgage banking, CMS Resources, SkillSoft, and performance management.
- Curriculum for all offerings is periodically reviewed and revised, ensuring that the courses are relevant and current. Surveys offer feedback on the value of the specific training. Employees post their training credits to the website. All content is reviewed before employees get credit for internal and external training as well as conference attendance. External programs are also utilized, and in some cases, provide various professional certifications.
- Senior managers, subject-matter experts, and trainers frequently travel to Hyderabad to facilitate and enhance the educational offerings; there were over 85 trips in 2014.

Berkadia sets a minimum target of 45 hours per year per employee. In 2014, employees averaged 89 hours of training globally, with Hyderabad employees averaging 95 hours (considerably above U.S. levels for other servicers we rank) and U.S. employees averaging 73 hours. During the first half of 2015, the primary, master, and special servicing teams averaged 28, 28, and 59 hours of training, respectively.

Systems and technology

Berkadia has well-integrated, efficient technology for its servicing requirements, and it operates with a high degree of system automation using an integrated array of applications. Its data warehouse is integrated with its Active Server Pages (ASP)-hosted mortgage loan accounting and servicing system, its special servicing system, and investor reporting and borrower website portals. Features of Berkadia's systems and technology include the following:

- McCracken Financial Solutions Corp.'s Strategy program is the system of record for primary/master servicing. Berkadia upgraded its system to Release 17.3 in late 2014 and migrated to 17.6 (the newest release available) in the third quarter of 2015.
- The company uses SmartTrack 2.0 to track tasks, process requests, and refer inquiries across various teams.
- Berkadia integrated CertInView as an insurance compliance monitoring program during 2014.
- AIMS, a proprietary application for special servicing, connects other internal systems and a reporting subsystem as

well. It includes a pooling and servicing agreement (PSA)-driven compliance module, a business plan module, a subcontracting service request and administration module, and an assumptions and consent request module.

- All the applications are integrated with each other and are connected to the company's data warehouse.
- Document imaging is fully supported, and all departments and regional offices use electronic file management applications, incorporating work flow tracking.
- Borrower and investor websites are provided.

Berkadia operates with sound data backup protocols. Disaster recovery and business resumption are tested every six months, more frequently than most servicers we rank. The company has agreements with vendors and other Berkadia office locations for alternate workspace and data restoration if needed. In December 2014, Berkadia moved its primary U.S. data center to TierPoint, a Tier 4 state-of-the-art disaster recovery facility in Norristown, Pa., and relocated its India disaster recovery site to Pune, India. The most recent disaster recovery tests were successfully completed in December 2014 in the Ambler, Pa. office and June 2015 for the Hyderabad office, in Pune.

Also, Berkadia utilizes data loss prevention technology that recognizes, captures, and reports inappropriate transmission of sensitive information, as well as removes access to external email accounts from the Berkadia network.

Internal controls

Audits. Berkadia follows a robust audit program that includes reviews by internal staff, external auditors, clients, and investors. Internal audits are geared toward all servicing and special servicing compliance requirements, operational controls, and testing. Features of Berkadia's internal audit department include the following:

- The internal audit department independently reports to the audit committee and board of managers.
- In 2014, USAP and Regulation AB audits were performed, based on contract terms for service agreements and PSAs, with no reported findings.
- Grant Thornton LLP performed platform-level Standards for Attestation Engagements (SSAE) 16 reviews (Service Organization Control [SOC] 1 and SOC 2 design of controls) in 2014, which cover the servicing platform and related technology, and there were no reported findings. For 2015, Berkadia will perform SOC 1 and SOC 2 (test and design of controls).
- The SOC 2 platform review covers data security, operational availability, processing integrity, and information confidentiality.
- Internal audits of cash disbursements, cash receipts, and servicing advances were completed since our last review. The auditors for each concluded that Berkadia has a satisfactory or better control environment.

Servicing audits are planned in advance and are geared toward the risk management of various servicing operations and cover cash controls as noted above (receipts and disbursements), investor reporting, loan administration/asset management, advancing, and documentation. In addition to formal audits, Berkadia employs strong QC processes, including measuring performance against departmental standard turnaround times and monitoring productivity results and accuracy of various servicing tasks.

Policies and procedures. Berkadia has an extensive, well-documented and well-maintained library of procedures for all servicing operations. The procedures not only incorporate the step-by-step operations, but also provide relevant forms and definitions for each activity. Policies and procedures are often written to address specific guidelines issued by partnering servicers. The procedures are online and updated regularly as required by process, system, or regulatory changes. Changes are conveyed to employees with appropriate training and follow-up QC and compliance reviews.

Vendor management. Berkadia engages several outside firms for various master/primary servicing and special servicing activities. Approved vendor lists are maintained for those asset-specific services. Vendor contracting is handled centrally for portfolio-wide operations (including Uniform Commercial Code [UCC] filings and tax service) and through asset managers with appropriate oversight and approval for asset-specific services (including property management, appraisal, and brokerage). Berkadia's asset management system provides centralized vendor lists, and the company prepares an annual vendor compliance report to determine if its vendors continue to meet the terms of their contractual arrangements. A subcontracting manager tracks engagements through the system's automated requests for service, competitive bidding (if applicable), issuance of standard contracts, and final completion of service.

Insurance. We believe Berkadia has acceptable directors and officers and errors and omissions insurance coverage. Management reported that it is not currently facing any servicing litigation matters.

Loan Administration--Primary Servicing

The subranking for primary loan administration is STRONG.

In 2012, Berkadia's primary servicing portfolio began to rebound from run-off that began in 2008, and it has maintained a fairly consistent level of UPB since 2013 (see table 5). As of June 2015, the majority of the \$230 billion (including master servicing) portfolio (57%) was broadly distributed across third-party investors (including a number of private-label relationships and a CMBS focused fee-for-service relationship that represents 30% of the portfolio); the next-largest investor client type is CMBS (26%) followed by Fannie Mae/Freddie Mac agency loans (9%). Portfolio volume growth has been driven by increased average loan sizes added to the platform in recent years (\$10.7 million at June 30, 2015, versus \$7.5 million as of Dec. 31, 2011), which have managed to offset unit growth declines.

Table 5

Primary Servicing Portfolio												
	June 30, 2015		Dec. 31, 2014		Dec. 31, 2013		Dec. 31, 2012		Dec. 31, 2011		Dec. 31, 2010	
	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.
Primary loans	224,523	21,080	229,325	22,204	227,479	24,004	182,481	23,284	163,796	21,902	179,922	24,736
Average loans size	10.7	--	10.3	--	9.5	--	7.8	--	7.5	--	7.3	--
Delinquent (%)												
30 days	0.26	--	0.44	--	0.34	--	0.50	--	0.86	--	1.64	--
60 days	0.07	--	0.08	--	0.16	--	0.26	--	0.56	--	0.47	--
90+ days	3.08	--	3.30	--	4.19	--	2.53	--	5.92	--	6.75	--
Total	3.41	--	3.82	--	4.69	--	3.29	--	7.34	--	8.86	--

Primary loan administration is centered around individual client relationship managers assigned to each loan. The portfolio includes all types of collateral (see table 6), many of which have complex loan structures. Berkadia's approach

to operations includes automating routine/back-office tasks as appropriate, which we believe has been successful. At the same time, the LPE ratio has steadily declined to 29 as of June 30, 2015, from the low- to mid-40s during 2010-2012 (see table 4), which is at the lower end of our ranked servicers. The lower level is offset by the comparative cost benefit of offshoring, which provides leverage to enhanced controls, allowing for more scrutiny and reviews of servicing data and reports.

Table 6

Portfolio Breakdown By Property Type And State(i)				
	Unpaid principal balance (mil. \$)	Unpaid principal balance (%)	No. of properties	Properties (%)
Type				
Multifamily	72,309	31.5	9,426	28.8
Retail	48,256	21.0	5,250	16.0
Office	45,134	19.6	2,170	6.6
Lodging	12,189	5.3	1,095	3.3
Industrial	8,905	3.9	1,771	5.4
All other	32,876	14.3	11,483	35.0
Defeased	10,111	4.4	1,569	4.8
Total	229,781	100.0	32,764	100.0
State				
CA	36,752	16.0	4,469	13.6
NY	25,331	11.0	1,537	4.7
TX	19,383	8.4	2,593	7.9
FL	16,550	7.2	2,420	7.4
IL	9,943	4.3	1,604	4.9
All other	111,710	48.6	18,572	56.7
Defeased	10,111	4.4	1,569	4.8
Total	229,781	100.0	32,764	100.0

(i)As of June 30, 2015.

The company uses automation to:

- Supplement complex third-party cash management arrangements;
- Maintain process efficiency; and
- Leverage the Hyderabad office with appropriate oversight and technology workflow applications.

New loan setup

Loan boarding is well-automated and includes in-depth procedures for secondary review. Features of the new loan setup team include the following:

- Loans are primarily boarded via electronic interface from origination and/or servicing systems under the control of the new loan setup team.
- The team consists of personnel in Hyderabad and the U.S.
- The Hyderabad setup staff performs initial data scrubbing and generates deficiency reports from the servicing system.
- Loan boarding requires a secondary review in the U.S. for control and validation.

- The U.S.-based team will manage the entire loan boarding process in some instances, such as loans with special issues, loans with complex waterfalls, and reboarding loans returned from special servicers.
- An extremely detailed monthly tracking report is produced, covering volumes, timeliness, and information accuracy.

Imaging and workflow applications aid in the boarding process, and PSA abstracts are incorporated in the servicing system. Welcome letters are system-generated and sent to the client relationship manager, who forwards it to the borrower.

Payment processing

Payment processing is handled by a separate team, in a highly automated process. Features of payment processing include the following:

- Approximately 100% of payments are processed electronically as 55% are received via Automated Clearing House, 27% via lockbox, and 18% via wire transfers.
- To maximize efficiency, Berkadia uses two third-party lockbox processing platforms, the data of which are downloaded to the servicing system.
- Adjustable-rate mortgage (ARM) audits are periodically performed to ensure correct rate indices and changes.
- Online banking software facilitates an automated custodial account reconciliation process.
- The servicing system automatically transfers funds daily between payment clearing and investor custodial accounts.
- The general ledger is interfaced with the servicing system.

The company has sound internal controls over payment posting and reconciliation.

Investor reporting

Berkadia has maintained efficient and effective investor reporting, remitting, and accounting processes with appropriate internal controls, and the company has experience with CMBS, life insurance company, GSE, and third-party investor clients. Separate staff members handle the bank account reconciliation, remittance, and investor reporting processes to maintain a proper segregation of duties.

- Investor reporting and accounting analysts are assigned workloads by investor or trustee/deal relationship.
- The servicing system is integrated with external banking software to facilitate outgoing investor wires and automatically reconcile custodial balances daily.
- All third-party reporting is handled electronically.

As of our latest review, there were no unreconciled items within investor custodial accounts and no instances of late reporting or remitting.

Escrow processing

Berkadia significantly leverages its operation in Hyderabad to handle a number of items, including vendor and borrower contacts for taxes, escrow reserves, and draw requests. Features of the escrow processing include the following:

- Approximately 57% of the total portfolio is escrowed for taxes and 43% for insurance.
- Specialists within loan administration both domestically and in Hyderabad handle aspects of escrow processing and reserves.
- A third-party vendor handles taxes on both escrowed and nonescrowed loans.
- Berkadia uses CertInView, a proprietary in-house insurance tracking solution and risk mitigation tool, for monitoring

and noncompliance reporting. The tool provides review consistency, eliminating document and requirement interpretation.

- Forced-placed coverage has a 120-day look back period. There were 96 loans on forced placed coverage as of June 2015.
- Automation tools assist in reserve analysis, including factors related to property tax increases depending on jurisdiction and tenant improvement reserves.
- Other collateral monitoring requirements, such as UCCs and letters of credit, are also part of the loan administration group.

Berkadia maintains an efficient and well-controlled function for insurance, real estate tax, and reserve administration. The company has a high level of automation and appropriate internal controls. The night shift in Hyderabad works along the U.S. staff and vendors during the daytime hours in the U.S. The U.S. staff generally handles resolution of exception items.

Asset administration

Separate areas within loan administration handle the collections and spreading of financial statements (with support from BSI) and the scheduling of property site inspections. Overall, procedures for these functions are properly managed with effective automation tools. Other features include the following:

- The servicing system and workflow application track open items.
- As of June 30, 2015, Berkadia analyzed 93% of 2014 annual operating statements received, which is relatively consistent with past experience, but slightly shy of the internal 95% target. As of the same date, Berkadia analyzed 98% of 2014 annual operating statements received from its CMBS portfolio.
- Third-party vendors conduct site inspections, which occur annually for accounts over \$2 million and biannually for all others.

Overall, Berkadia has good controls, ensuring that financial statements and inspections comply with the company's policies, servicing agreements, and loan documents.

Portfolio administration

Portfolio surveillance is handled through the collateral administration department, encompassing teams of asset managers aligned by investor and assigned to specific loan pools. Since our last review, CMBS asset management and surveillance efforts have transitioned to the Ambler and Hyderabad offices. Surveillance analysts serve as the point of contact for trustees, bond holders, and rating agencies. Other features of surveillance include the following:

- Asset managers review principal and interest and property protection advances, maintain watchlists, and monitor specially serviced loans.
- Watchlist triggers are automated by the servicing system, which also provides manual flagging.
- In addition to the standard Commercial Real Estate Financial Council watchlist, Berkadia maintains other specific client-driven watchlists. Automated watchlist logic is used to place loans on the watchlist for deficient financials, low occupancy levels, and/or negative inspection reports. As of June 30, 2015, there were 2,829 loans on the watchlist.
- The surveillance team meets monthly to review each transaction's performance. They focus on problem loans, 30-day delinquencies, loans in special servicing, and advancing needs and recoverability.
- Analysts also prepare bond impact analyses associated with delinquencies and advancing to estimate bond interest shortfalls, proactively communicate with rating agencies, and monitor the trustee's waterfall distributions.
- Berkadia removes a loan from the watchlist if the negative conditions are cured.

Berkadia maintains a sound portfolio surveillance function that proactively examines asset and portfolio-level performance. It provides a well-detailed investor website that contains deal- and loan-level performance data.

We track servicers' volume and average response times for processing borrower requests, including assumptions, leasing consents, and defeasances that often require third-party consent. Berkadia's internal approval times for CMBS assumptions and leasing consents lagged behind a peer group of primary servicers during the first half of 2015. Internal approval time for defeasance reviews, of which Berkadia performed more than 100 during the first six months of 2015, is largely similar to peers. In the aggregate, Berkadia, as primary servicer, processed more than 300 consents during the first half of 2015, and we believe its workflow application to respond to such requests provides a well-controlled process.

Early stage collections

Berkadia takes proactive measures to initiate collection efforts by contacting borrowers the day after delinquency or grace period depending on the service agreement. Other features of the collections group include:

- Client relationship managers monitor daily delinquency reports and call borrowers to obtain information surrounding the cause of the delinquency and anticipated payment cure date.
- Comments are tracked on the servicing system.
- In instances of sustained delinquency, such as insufficient or disrupted cash flows because of weather events/insurance, the relationship manager will refer the loan to the assigned asset manager for follow up.
- Default notices are generated at 30 and 45 days past due, and depending on circumstances, further actions are taken--such as demand letters--at 60 days past due.

Loan Administration--Master Servicing

The subranking for master servicing loan administration is STRONG.

We believe Berkadia is an effective master servicer: As of June 30, 2015, it monitored 20 subservicers, who serviced 479 loans containing \$5.3 billion in UPB. However, the subservicer portfolio has continued to decline in recent years (see table 7), as loan run-off has greatly exceeded new master servicing loan activity.

Table 7

Master Servicing Portfolio													
	June 30, 2015		Dec. 31, 2014		Dec. 31, 2013		Dec. 31, 2012		Dec. 31, 2011		Dec. 31, 2010		
	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	Unpaid principal balance (mil. \$)	No.	
Master (SBO) loans	5,257	479	6,017	625	7,235	1,020	9,585	1,422	12,062	1,828	13,336	1,204	
Subservicers	--	20	--	21	--	25	--	29	--	33	--	33	
Average loan size	11.0	--	9.6	--	7.1	--	6.7	--	6.6	--	11.1	--	
Delinquent (%)													
30 days	0.04	--	0.43	--	0.15	--	2.34	--	1.12	--	1.09	--	

Table 7

Master Servicing Portfolio (cont.)												
60 days	0.39	--	0.02	--	0.12	--	0.22	--	0.16	--	0.03	--
90+ days	0.00	--	0.09	--	1.96	--	5.69	--	5.93	--	1.47	--
Total	0.43	--	0.53	--	2.23	--	8.26	--	7.20	--	2.58	--

SBO--Serviced by others.

A subservicer oversight group oversees all aspects of an individual subservicer's compliance. It reviews subservicers' monthly activity and quarterly compliance certificates, and it is the liaison for channeling borrower requests, financial statements, and inspection reviews to appropriate areas within Berkadia. Its risk and compliance department manages the subservicer audit program. This department also reviews compliance certifications against PSA requirements.

New loan setup

Berkadia follows the same procedures for boarding new subserviced loans on its servicing system. Because these loans are all serviced by other servicers, the setup process is essentially via electronic file downloads. Other features of new loan setup include the following:

- The subservicing team validates data consistency between the subservicers system data and the loan record information downloaded to Berkadia's system.
- Loans are set up for "shadow servicing" to record loan-level principal and interest payment records; tax and insurance information is not loaded at the loan level but monitored via quarterly officer certificates and monthly subservicer reports.
- Loans with complex waterfalls are reviewed by senior staff for accuracy.
- The monthly new loan setup tracking report includes information on subserviced loans covering volumes, timeliness, and accuracy of information.
- Electronic copies of pertinent loan documents are also obtained and referenced within the imaging application.

Payment processing

Berkadia shadow-posts principal and interest loan-level activity within its subserviced portfolio from electronic uploads by subservicers. It does not require its subservicers to submit forecasted remittance amounts before the actual remittance date because it closely monitors delinquencies and has appropriate controls over advancing under master servicer investor reporting.

Escrow administration

Berkadia obtains subservicer quarterly certifications to ensure that real estate taxes, property insurance, UCC renewals, and reserve accounts remain in compliance. Berkadia's tax service contract includes the master servicing portfolio so it can verify tax payments and update its servicing systems' records.

Subservicer oversight (asset and portfolio administration)

Berkadia has good controls over subservicer compliance that include formal onsite and desk audits. The subservicer group performs monthly compliance reviews for timeliness of remittances, watchlist items, financial statement collections and analysis, and property inspections. Other features include:

- A monthly tracking report monitors the subservicers' completion and submission of their portfolio reconciliations, and Berkadia reconciles monthly each subservicer's loan remittance to match its own system records.

- Berkadia monitors each property's performance by reviewing financial statement spreads and inspection reports from subservicer uploads.
- Borrower requests processed by the subservicer are tracked by the company's subservicer team and managed through the workflow tracking system for response in its master servicer function.
- Annually, the firm performs desktop (five performed during 2014) and onsite compliance audits (two performed during 2014). Subservicer audits entail a detailed pre-audit questionnaire about the subservicer's operations.

The onsite audits cover all core servicing functions using file samplings, system reports, and staff interviews. We believe these protocols provide an appropriate level of risk mitigation, particularly when combined with its ongoing subservicer interaction and compliance monitoring practices.

Master servicer investor reporting

As in primary investor reporting, all reporting is accomplished via electronic file deliveries and wire transfers. The additional activities for master servicer reporting include combining Berkadia's subserviced portfolios with its own directly serviced (primary) loans and determinations for advancing. Other features of investor reporting include the following:

- Monthly investor reporting occurs within the servicing operations group for CMBS, commercial real estate collateralized debt obligation (CRE-CDO), and private-label investors, as well as the individual servicing groups for agency and life company portfolios.
- The investor reporting manager within each group reviews the total remittances--primary plus subserviced loans--and supporting reports for accuracy and other information such as complete watchlist information.
- The review also helps the committee determine if the loan should be transferred to the special servicer.
- The monthly advance review committee reviews delinquent loans to determine if it should continue to make advances. The committee also discusses the results of the recoverability analysis based on data provided by special servicers, external market information, and Berkadia's own internal analysis at both the asset and pool level.
- Advancing decisions are based on individual loan facts and circumstances, not a static formula.
- Waterfalls are closely monitored regarding advancing, recoverability, and notifications to trustees and rating agencies.

Berkadia has proactive procedures for master servicer reporting that includes advance determination analysis and conservative advance limits. The CMBS surveillance group monitors loan-level advances for each CMBS transaction using the asset management database for tracking advance details. Dedicated portfolio management teams oversee the special servicing transfer process.

Loan Administration--Special Servicing

The subranking for commercial mortgage special servicing loan administration is ABOVE AVERAGE.

On July 31, 2013, Berkadia transferred its legacy CMBS special servicing portfolio to KeyBank as part of a larger transaction where KeyBank engaged Berkadia to perform certain primary servicing tasks on a \$100 billion commercial loan servicing portfolio, including \$57 billion acquired from Bank of America. The legacy CMBS special servicing portfolio was approximately \$560 million in active specially serviced loans and \$9 billion in loans where Berkadia was the named CMBS special servicer. Furthermore, this significant decrease in volume resulted in staff reductions

primarily in Berkadia's Dallas office.

The aforementioned transaction included a CMBS specific option, whereby if Berkadia were appointed special servicer, KeyBank has the opportunity to assume those responsibilities, which has limited its participation in new CMBS special servicing business during the past two years. This arrangement is scheduled to expire in 2016.

Since the transaction, Berkadia has continued performing special servicing and asset management for a small number of assets. We believe the company has maintained adequate staffing, special servicing systems (e.g., AIMS) and procedures for its current volume.

Berkadia is currently the named special servicer on four newer vintage single-asset CMBS transactions approximating \$1.2 billion in UPB. As of June 30, 2015, it was also actively special servicing 25 small-balance loans, including three real estate owned (REO) assets, containing \$9 million in UPB from a handful of early vintage transactions (see table 8).

Table 8

Special Servicing Portfolio														
June 30, 2015			Dec. 31, 2014				Dec. 31, 2013			Dec. 31, 2012				
Unpaid principal balance (mil. \$)		No.	Average time in special servicing (mos.)		Unpaid principal balance (mil. \$)		No.	Average time in special servicing (mos.)		Unpaid principal balance (mil. \$)		No.	Average time in special servicing (mos.)	
Active inventory														
Loans	8.3	22	37.5	2.7	17	45.7	19.6	21	32.9	867.2	85	24.6		
Real estate owned	0.9	3	5.5	0.0	0	0.0	0.0	0	0.0	715.8	30	38.6		
Total	9.1	25	33.7	2.7	17	45.7	19.6	21	32.9	1,583.1	115	28.3		

Note: Average age reflects time in months from the date the loan first became specially serviced to the reporting date.

Loan recovery and foreclosure management

Historically, Berkadia has proactively handled newly transferred loans to special servicing. Other features include the following:

- Asset managers complete full file reviews, perform property inspections, assemble local market data, and develop the loan resolution plan no later than 90 days after transfer.
- The asset management system houses all work-out plans and includes net present value (NPV) analysis for various scenarios.
- Asset managers engage vendors through approved lists that are also tracked within the asset management application, which also provides for timeline monitoring.
- Plans are presented to a special servicing committee for approval with levels of delegated authority.
- Work-out plans are updated every six months, or sooner, and implemented and monitored on an ongoing basis to ensure adherence to plan objectives.
- If warranted, properties are recommended for foreclosure and an REO business plan is prepared within 90 days of taking title.
- The compliance area and contracting/accounting area also review the progress of plans and adherence to contractual servicing requirements.

Given the current portfolio size, Berkadia's recent resolution activity has been limited (see table 9) and asset sizes have been small. The average outstanding loan amount of the assets resolved during the six months ending June 2015 was \$287,000.

Table 9

Total Special Servicing Portfolio--Loan Resolutions												
June 30, 2015			Dec. 31, 2014			Dec. 31, 2013			Dec. 31, 2012			
Unpaid principal balance (mil. \$)	No.	Average time in special servicing (mos.)	Unpaid principal balance (mil. \$)	No.	Average time in special servicing (mos.)	Unpaid principal balance (mil. \$)	No.	Average time in special servicing (mos.)	Unpaid principal balance (mil. \$)	No.	Average time in special servicing (mos.)	
Resolutions												
Loans	2.0	7	14.4	2.7	6	33.1	283.6	29	24.5	2,076.2	90	13.8
Foreclosed loans	--	--	--	14.2	1	6.4	71.6	3	4.8	100.1	16	22.5
Total	2.0	7	14.4	16.9	7	29.3	355.2	32	22.6	2,176.3	106	15.1
Resolution breakdown												
Returned to master	1.6	4	2.3	0.3	4	38.9	231.0	9	29.5	1,302.4	20	13.0
Full payoffs	--	--	--	2.5	2	21.5	18.9	16	22.2	552.4	35	12.6
DPO or note sale	0.4	3	30.4	--	--	--	33.7	4	22.1	221.4	35	15.4
Foreclosed loans	--	--	--	14.2	1	6.4	71.6	3	4.8	100.1	16	22.5
Total/average	2.0	7	14.4	16.9	7	29.3	355.2	32	22.6	2,176.3	106	15.1

DPO--Discounted payoff.

Berkadia's foreclosure process is soundly controlled and well managed. Recommended foreclosure actions initiate REO resolution plans, which include a bidding process for property management and brokers. Detailed pre- and post-foreclosure checklists help ensure that all time-sensitive issues surrounding the asset, such as environmental reports and appraisals, are completed before taking title.

REO management and disposition

Asset managers within special servicing monitor property managers and brokers, implement approved disposition plans, review property cash flow activity and disbursements, and negotiate lease and sale transactions for committee approval. As part of the REO management process, the asset managers prepare a formal property business plan within the first 90 days of taking title. All REO business plans and any subsequent transaction-specific requests are presented for committee approval.

Table 10

Total Special Servicing Portfolio--REO Sales

	June 30, 2015			Dec. 31, 2014			Dec. 31, 2013			Dec. 31, 2012		
	Amount (mil. \$)	No.	Average REO hold period (mos.)	Amount (mil. \$)	No.	Average REO hold period (mos.)	Amount (mil. \$)	No.	Average REO hold period (mos.)	Amount (mil. \$)	No.	Average REO hold period (mos.)
Estimated market value	--	--	--	8.9	1	5.1	78.3	34	16.3	171.3	63	11.1
Net sales	--	--	--	12.3	--	--	80.6	--	--	168.3	--	--
Sale/market value (%)	--	--	--	137.2	--	--	102.9	--	--	98.2	--	--

REO--Real estate owned.

Sale offers must meet the parameters of the approved REO plan or a subsequent committee reviews the alternate offer. Asset managers coordinate the closing process in conjunction with legal counsel and an asset administrator who ensures that all documents are consistent with the approvals and update the information in the corresponding systems. Since our last visit, Berkadia had experienced minimal REO sales activity (see table 9), and we do not anticipate any near-term increase in the portfolio.

REO accounting and reporting

Berkadia has defined procedures within special servicing to oversee accounting and reporting activities:

- When a property is converted to REO, an asset manager immediately initiates the process to establish and maintain control of any cash generated by the property.
- Control over REO cash and operating activity is accomplished by monitoring performance against an approved operating and capital expenditure budget, scrutiny of the monthly property reporting package and funding request, and control over property manager bank accounts. These controls are the joint responsibilities of the asset manager and a designated administrator that coordinates cash movement and other REO bank account activities. The special servicing group does not directly handle cash; that responsibility resides with Berkadia's accounting department. In addition, Berkadia's finance group reviews the operating reports for the subject properties in the current portfolio.
- Property managers receive manuals for reporting guidelines and standard formats; all accounting is handled through a single bank checking account for revenue and expenses on each property.
- Property managers submit their financial data electronically, and the asset manager rechecks the bank's operating account reconciliation.

We believe Berkadia's REO accounting and reporting would be better controlled if there were dedicated accounting employees who would reconcile monthly bank accounts, rather than the asset manager. However, given the minimal volume of REO assets currently under management, the declining portfolio, and the independent review by Berkadia's finance group, we believe the current procedures are adequate at the existing ranking level. Berkadia has indicated that they would add the requisite accounting resources as operating properties in the portfolio increased.

Legal department

The special servicing operation is supported by an in-house attorney. The legal division maintains a list of approved outside attorneys and uses standard engagement letters. However, the assigned asset manager must review legal invoices before payment. We believe the legal function is adequately controlled.

Financial Position

Berkadia's financial position is SUFFICIENT, which reflects Standard & Poor's 'AA/Watch Neg' rating on BRK as well as its 'BBB-/Stable' rating on LUK.

Related Criteria And Research

Related Criteria

- Revised Criteria For Including RMBS, CMBS, And ABS Servicers On Standard & Poor's Select Servicer List, April 16, 2009
- Servicer Evaluation Ranking Criteria: U.S., Sept. 21, 2004

Related Research

- Berkadia Commercial Mortgage LLC Commercial Rankings Affirmed; Special Servicer Ranking Outlook Revised To Negative, Oct. 30, 2015
- Select Servicer List, Sept. 11, 2015

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